Middle East Healthcare Co

2Q2019 Results Review

29 August 2019

Patient Volume Thinning

SAR 22 — 12-Month Target price

Sell — Recommendation

MEAHCO reported 2Q19 EPS of SAR 0.13 (-64% Y/Y), missing our SAR 0.16 forecast as costs continued to rise from salaries (+8% Y/Y). While receivables are being collected from MoH with some regularity (paid-up until Jan-2019), the decline of referrals from this key source is impacting volumes – business mix at 28% from 33%. Management is targeting topline resuscitation through increased focus on cash and insurance clients. However, the impending cost pressure is difficult to ignore as Dammam is commissioned in 4Q19. Reiterate Sell and SAR 22 target price, representing 14.3x 2020E EV/EBITDA.

Ongoing renos impacting inpatients

Total revenues during the quarter edged up +2% Y/Y to SAR 353 mln, ahead of our SAR 335 mln estimate. 1H figures indicate -9% decline in inpatients but +2% growth in outpatients. While renovations completed in Asir, Riyadh is undergoing expansion and upgrade – dragging group utilization rate to 65% vs. optimum level of 75-80%. Subsequent facilities are targeted through 2021 at a total cost of SR 100 mln. Management believes these expenditures will improve patient experience, driving topline growth. Other factors cited for weaker revenues are market saturation in Jeddah and relatively smaller patient pool in other regions, however the decline in MoH referrals is concerning. The Company is receiving critical cases from MoH, which command higher pricing but lower volumes. Outpatient revenue improved on strong uptake from Beverly Clinics.

Further cost increase on horizon

Gross margin compressed to 29% from 34% during year ago period on higher caregiver costs and expat fees while SG&A gained some +12% Y/Y. Cost pressure appears unlikely to ease considering Dammam commissioning in 4Q19 entails escalating depreciation and hiring costs. Management believes Dammam should breakeven in under 1.5 years, propelled by corporate clients (Aramco, petrochems) and somewhat differentiated service offering from upcoming capacity addition (Mouwasat, Sulaiman Habib). Note that Hail is expected to breakeven by yearend, some 2 years post-launch.

Earnings disappoint, multi-pronged strategy announced

MEAHCO earnings have dramatically declined from a quarterly average of SAR 85 mln, down to SAR 12 mln (-64% Y/Y). Various factors contributed to this reversal of fortune, including MoH exposure, expat outflow, escalating salaries and fees. Management has identified multi-pronged strategy targeting optimized customer mix (substituting MoH business with cash and insurance), offshoring costs, expansion into Africa and Gulf region and improving loss rate from reductions, which can potentially yield savings in the range of 10-20%.

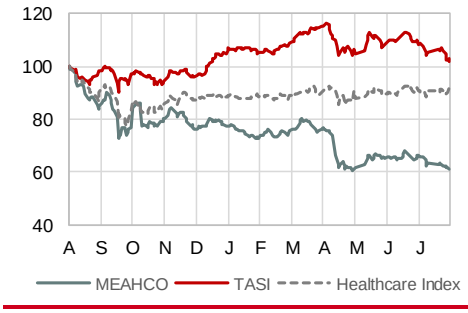
SAR mln	2Q19	2Q19E	2Q18	*Y/Y Chg*	1Q19	*Q/Q Chg*	*Variance*
Sales	353	335	346	*2%*	350	*1%*	*5%*
Gross profit	103	97	117	*-12%*	102	*1%*	*6%*
Gross margin	*29%*	*29%*	*34%*		*29%*		
EBITDA	34	47	53	*-36%*	41	*-18%*	*-28%*
EBITDA margin	*10%*	*14%*	*15%*		*12%*		
Operating profit	8	15	32	*-76%*	18	*-59%*	*-48%*
Operating margin	*2%*	*4%*	*9%*		*5%*		
Net income	12	15	34	*-64%*	15	*-16%*	*-19%*
Net margin	*3%*	*4%*	*10%*		*4%*		
EPS (SAR)	0.13	0.16	0.37	*-64%*	0.16	*-16%*	*-19%*

Stock Details		
Last Close Price	SAR	25.50
Upside to target	%	(13.7)
Market Capitalization	SAR mln	2,347
Shares Outstanding	mln	92
52-Week High	SAR	42.00
52-Week Low	SAR	24.90
Price Change (YTD)	%	(21.4)
3-Mth ADTV	thd	255
EBITDA 2019E	SAR mln	190
Reuters / Bloomberg	4009.SE	MEH AB

SAR mln	2018	2019E	2020E
Revenues	1,391	1,345	1,364
Gross Margin	*36%*	*29%*	*29%*
EBIT	163	64	63
Operating Margin	*12%*	*5%*	*5%*
Net Income	172	61	57
Net Margin	*12%*	*5%*	*4%*
EPS (SAR)	1.87	0.67	0.62
DPS (SAR)	-	-	-

Price Multiples	2018	2019E	2020E
P / E	13.6x	38.3x	41.1x
EV / EBITDA	12.3x	16.4x	16.0x
P / S	1.7x	1.7x	1.7x
P / B	1.6x	1.8x	1.7x

1-Year Share Performance (rebased)



Source: Bloomberg, Tadawul, SFC

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